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IN THE

Supreme Court of the United States

October Term, 1945 No. 892 18

WALTER J. ROTHENSIES, Individually, and as United States Collector of Internal Revenue for the First District of Pennsylvania,

Petitioner

v.

THE ELECTRIC STORAGE BATTERY COMPANY, a Corporation

Brief for Respondent in Opposition to Petition for a Writ of Certiorari

LAURENCE H. ELDREDGE,
CHARLES C. NORRIS, JR.,
NORRIS, LEX, HART & ELDREDGE,
1500 Walnut Street,
Philadelphia 2, Penna.
Attorneys for Respondent,

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WALTER J. ROTHENSIES, Individually, and as United States Collector of Internal Revenue for the First District of Pennsylvania, *Petitioner*

v.

THE ELECTRIC STORAGE BATTERY COMPANY, a corporation.

BRIEF FOR THE RESPONDENT IN OPPOSITION.

I. OPINIONS OF COURTS BELOW.

Electric Storage Battery Company v. Rothensies (1944) 57 F. Supp. 731 (R. 5a-17a).

Electric Storage Battery Company v. Rothensies (CCA3-1945) 152 F. 2nd 521 (R. 2-9).

II. JURISDICTION.

1. The jurisdiction of this Court is invoked under the Judicial Code, Section 240 (a), as amended by the Act of February 13, 1925, ch. 229, 43 Stat. 938 (28 USCA § 347).

2. The judgment of the Circuit Court of Appeals was entered on November 27, 1945 (R. 9).

III. QUESTION PRESENTED.

Where the Government illegally collected money prior to 1928 from a corporation under the guise of excise taxes, part of which it later refunded and made a deficiency income and excess profits tax assessment on the refund, is not the corporation entitled to recoup the moneys not refunded against the deficiency assessment?

IV. STATEMENT OF THE CASE.

During the seven years between March 1, 1919, and February 28, 1926, the Government illegally exacted 84 monthly payments from the respondent as excise taxes on the respondent's sales of electric storage batteries upon the erroneous theory that the batteries were parts of automobiles. All of the assessments were upon the same types of batteries. In 1935, as a result of litigation instituted by the respondent, the Government refunded the last 45 payments, these being the payments made between 1922 and 1926 (R. 2). The Government treated this refund as income in the year 1935 and assessed a deficiency income and excess profits tax on the refund which, together with interest, amounted to $229,805.34 (R. 6a). The respondent sought to recoup against this assessment the first 39 monthly payments which had been made between 1919 and 1922 and which the respondent had not asked to recover in the prior litigation because of the bar of the statute of limitations (R. 2). The total amount of the payments made between 1919 and 1922 and which the respondent had absorbed itself is $534,205.04 (R. 6a). After the Government rejected the respondent's argument that it had a defense by way of recoupment to the entire deficiency assessment, the respondent paid this additional tax to the petitioner under protest (R. 2). After a claim for refund was denied, this suit was instituted to recover the payment and to obtain an adjudication of the validity of the recoupment defense (R. 2).

The money the respondent paid to the petitioner and which it seeks to recover from him in this litigation was paid by him to the Treasurer of the United States, as required by law: 26 U.S.C. § 3950. The moneys the respondent seeks to recoup were also paid by the Collector to the Treasurer of the United States, as required by law. (R. 20a-21a).

The District Court found that even after the Government is given credit for the respondent's income tax savings arising out of credits taken for the payment of all the excise taxes, the Government still has in its hands more than the amount of the 1935 deficiency tax assessment. (R. 17a). The following calculation shows the situation exactly:

Respondent's 1919-1922 net payments of excise taxes		$534,205.04
Respondent's income tax savings on above	$178,691.52	
Respondent's income tax savings on 1922-1926 payments	139,668.83	
		318,360.35
Net overpayment withheld by Government		$215,844.69
Additional 1935 income and excess profits taxes demanded and collected by Government		198,023.87
Overpayment by respondent after recoupment		$17,820.82

Although the total deficiency assessment paid in 1938 and based on the 1935 refund was $229,805.34, this was made up of additional tax of $198,023.87 plus interest thereon to the date of payment in 1938 of $31,781.47.

We disagree with the statement on page 6 of the petition that "The District Court held that the deficiency in 1935 income and excess profits tax was properly assessed

and collected, . . ." The Court held that the tax was properly assessed but that there was no right to collect any of the assessment because respondent's right of recoupment was a defense to the entire deficiency claim, (R. 13a), and the Circuit Court of Appeals agreed. (R. 8).

V. ARGUMENT.

SUMMARY.

Point 1. The common law doctrine of recoupment as applied in actions at law for more than a century is applicable to the present facts.

Point 2. There is no basic inconsistency or confusion in the decisions of this Court when properly analyzed and understood.

Point 3. Sections 608(a) and 609(b) of the Revenue Act of 1928 do not destroy respondent's substantive right of recoupment because (a) they do not purport to affect the jurisdiction of Federal Courts and (b) they do not destroy a substantive right of recoupment which a taxpayer had on their effective date.

Point 4. The rule that a taxpayer may not recover from one Collector of Internal Revenue moneys wrongfully paid to a predecessor collector has no application to the present case because the respondent only seeks to collect from the petitioner moneys paid to him which he had no right to demand or collect.

Point 1.

The common law doctrine of recoupment as applied in actions at law for more than a century is applicable to the present facts.

The petitioner's first reason for his petition is that the decision is "an unwarranted extension of the principle of the *Bull* case."

In **Bull v. United States (1935) 295 U. S. 247,** this Court held that the common law doctrine of recoupment was applicable to the facts there presented. The Court did not purport to set forth the limits of its application other than saying, "recoupment is in the nature of a defense arising out of some feature of the transaction upon which the plaintiff's action is grounded." (Page 262). The Court did not there define the word "transaction" but in a closely analogous situation the Court said in **Moore v. New York Cotton Exchange (1926) 270 U. S. 593, 610:** "'Transaction' is a word of flexible meaning. It may comprehend a series of many occurrences, depending not so much upon the immediateness of their connection as upon their logical relationship." In the leading case of **Stow v. Yarwood (1853) 14 Ill. 424, 426-27,** the Court said that recoupment "adjusts by one action adverse claims growing out of the same subject matter. . . . It is not necessary that the opposing claims should be of the same character . . . It is sufficient that the counterclaims arise out of the same subject matter, and that they are susceptible of adjustment in one action."

The recoupment doctrine came into the law to promote justice and should be liberally applied to accomplish that end wherever that can be done without undue procedural or administrative difficulty and no rule of public policy prevents it. Its convenient application to this case to enable the respondent to derive a benefit from the more than half million dollars of its money, originally obtained by duress (R. 19a), which the Government holds is in no sense an "unwarranted extension" of the doctrine of recoupment, as the careful analysis and documentation in Judge Goodrich's opinion shows: (R. 3-5).

Point 2

There is no basic inconsistency or confusion in the decisions of this Court when properly analyzed and understood.

Point 3

Sections 608(a) and 609(b) of the Revenue Act of 1928 do not destroy respondent's substantive right of recoupment because (a) they do not purport to affect the jurisdiction of Federal Courts and (b) they do not destroy a substantive right of recoupment which a taxpayer had on their effective date.

In *Bull v. United States*, supra, this Court held that a taxpayer could recoup against the Government's claim for valid taxes a tax which he had erroneously paid but could not recover back because of the statute of limitations. In so holding, this Court "permitted the taxpayer to accomplish indirectly what it could not do directly," which is the complaint made in the present case on page 10 of the petition. This indirect accomplishment is the inevitable result of the application of the recoupment rule in any case. In the *Bull* case the taxpayer was permitted to assert a right of recoupment which was created prior to the enactment of the Revenue Act of 1928 in litigation which was not started until *after* the effective date. In **McEachern v. Rose (1937) 302 U. S. 56** this Court held that after the enactment of Sections 607 and 609(a) of the Revenue Act of 1928 (which are not the sections relied on by petitioner), *the Government* could not credit against a taxpayer's overpayment an unpaid tax whose collection was barred by limitation (and which in fact did not become due until after the enactment of the 1928 Act). In the *McEachern* case the defense did not set up a plea of recoupment but alleged that in view of the fact that the taxpayer was suing in *indebitatus assumpsit*, "it would be unconscionable for the plaintiff to be allowed any recovery." The Circuit Court of Appeals sustained the Government's defense upon the theory that in view of the historical development of indebitatus assumpsit, the action "may not be used to obtain money which the plaintiff ought not, in good conscience, to have back:" 86 F. 2nd 231, 233. We submit that when this

Court decided that case, it did no more than hold that in a suit by a taxpayer to recover an overpayment *which the statute entitles him to receive*, the Government cannot raise the equitable defense that keeping the overpayment does not result in unjust enrichment. This is certainly the view which was argued strongly to the Court in the brief of the *amicus curiae*, particularly on pages 7 and 8 thereof. On the other hand, where the taxpayer is resisting the collection of a tax under the pleaded defense of recoupment, *Bull v. United States* is the controlling authority and it was cited with apparent approval by this Court six years after the decision in the *McEachern* case: **Commissioner v. Gooch M. & E. Co. (1943) 320 U. S. 418, 421.**

The petitioner has not cited a single case in which a taxpayer who has clearly proved the Government had his money has not been permitted to recoup it where the elements of recoupment were present. The two decisions of the Court of Claims cited on page 11 of the petition are not at all in direct conflict with the decision in this case. Those are both cases in which the taxpayer did not prove that he had ever made a true overpayment out of which any right of recoupment could arise and, in addition, different transactions were probably involved, so no rule of recoupment could be applied. There is language, however, in the opinions which shows that the Court of Claims failed to see the distinction between cases falling within the rule of *McEachern v. Rose* and those falling within the rule of *Bull v. United States*. There is definitely no conflict presented to this Court in the present petition for certiorari.

A second reason why the Revenue Act of 1928 has no application to the present litigation is that when the Government forced the respondent to make payments to it in 1919, 1920, 1921 and 1922, at the moment each illegal exaction was paid, a legal right to get it back arose. That right continues to exist and may be asserted defensively in a plea of recoupment. That it is a valuable substantive

right is evident: it constitutes a complete defense to a deficiency assessment claim of $229,000. Surely a 1928 statute containing directions to the Commissioner concerning "credits" and "refunds" did not destroy the respondent's existing right to plead recoupment. At the most, it did no more than close the Commissioner's ear to such an argument, and require the respondent to resort to a Court possessing general equity jurisdiction, to assert his right of recoupment. A statute will not be construed as destroying an existing right unless the legislative intent to do so is expressed in clear and unmistakable language, and even then the statute faces constitutional obstacles: **50 American Jurisprudence 500.** "Every reasonable doubt is resolved against a retroactive operation of a statute": **Valleytown Tp. v. Women's Catholic Order (CCA 4, 1940), 115 F. 2d 459, 462; U. S. v. St. Louis etc. Ry. Co. (1926), 270 U. S. 1; Hassett v. Welch (1938), 303 U. S. 303; Claridge Apartments Co. v. Commissioner (1944) 323 U. S. 141.**

Point 4

The rule that a taxpayer may not recover from one Collector of Internal Revenue moneys wrongfully paid to a predecessor collector has no application to the present case because the respondent only seeks to collect from the petitioner moneys paid to him which he had no right to demand or collect.

The respondent sued the petitioner to recover from *him* the sum of $229,805.34 which had been paid to *him* on December 3rd, 1938. The theory is that *he* illegally collected this money as Collector of Internal Revenue because no money was owing to the Government by the respondent. The judgment of the Court below is that the respondent is entitled to recover back from the petitioner the money paid to *him*. The judgment does not require him to pay back moneys paid to any other Collector. The petitioner's argument on page 12 of his petition ignores the facts in the

case and the fact that in tax litigation the position of the parties to the suit is generally the reverse of that in ordinary litigation. The respondent could have asserted the defense of recoupment if the Government had instituted suit to collect the 1935 deficiency. *Bull v. United States* is authority for the proposition that the respondent did not worsen its position by paying the 1935 deficiency assessment and suing the Collector to whom that payment was made to get the money back again.

VI. CONCLUSION.

The decision of the Circuit Court of Appeals in this case is correct; there is no conflict of circuits; the case does not involve an important question of Federal Law which has not been, but should be, settled by this Court, or the decision of a Federal question in a way probably in conflict with applicable decisions of this Court. On the contrary, the decision is in accord with the settled common law relating to recoupment and with the decision of this Court in *Bull v. United States*, and the petition should be denied.

Respectfully submitted,

LAURENCE H. ELDREDGE,

CHARLES C. NORRIS, JR.,

Attorneys for Respondent.